Christine A. Varney
+1-212-474-1140
cvarney@cravath.com

Margaret T. Segall
+1-212-474-1231
msegall@cravath.com

Daniel K. Zach
+1-212-474-1818
dzach@cravath.com

FTC/DOJ Make Increasing Antitrust Scrutiny of Private Equity a Top Priority

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Historically, acquisitions by private equity ("PE") firms have not raised significant antitrust issues unless PE firms owned one or more portfolio companies in a market and sought to buy a significant competitor. PE firms were often able to make multiple, small acquisitions in fragmented markets without raising concerns by U.S. antitrust enforcers, and, after such transactions, they often did not need to worry about how the ongoing operation and management of their portfolio companies were affected by antitrust laws. Recent statements by officials at the Federal Trade Commission ("FTC") and Antitrust Division of the U.S. Department of Justice ("DOJ"), as well as recent agency actions, indicate that enforcers are changing their approach to evaluating acquisitions and other practices by PE firms.

For example, FTC Chair Lina Khan wrote recently that "Antitrust enforcers must be attentive to how private equity firms' business models may in some instances distort incentives in ways that strip productive capacity, degrade the quality of goods and services, and hinder competition."[1] She went on to explain that, "serial acquisitions or 'buy-and-buy' tactics can be used by private equity firms and other corporations to roll up sectors, enabling them to accrue market power and reduce incentives to compete, potentially leading to increased prices and degraded quality."

In response to these concerns, the U.S. antitrust enforcement agencies have indicated they plan to:

- Utilize new tools to crack down on perceived "stealth acquisitions" and "roll-ups" by PE firms;
- Evaluate new approaches to analyzing acquisitions by PE firms; and
- Increase enforcement of Section 8 of the Clayton Act, which prohibits interlocking directorates.

Going forward, PE firms should expect increased antitrust scrutiny of their acquisitions and the management of their portfolio companies. To engage effectively with antitrust enforcers in this changing environment, PE firms should work closely with antitrust counsel to ensure they are aware of and account for all important developments in this new area of agency focus.

FTC UTILIZING NEW TOOLS TO ADDRESS PRIVATE EQUITY "STEALTH ACQUISITION" AND "ROLL-UP" CONCERNS

On June 13, 2022, the FTC announced a settlement that allowed JAB Consumer Partners ("JAB") to move forward with its $1.1 billion acquisition of SAGE Veterinary Partners ("SAGE").[2] JAB is a PE firm and parent company to Compassion-First Pet Hospitals and National Veterinary Associates, Inc. During its investigation, the FTC determined that a JAB/SAGE transaction would combine the only two

providers of specialty and emergency veterinary services in Austin, Texas; San Francisco, California; and Oakland, Berkeley and Concord, California.[3] To resolve its concerns, in addition to requiring clinic divestitures in these geographic markets, the FTC required JAB to accept broad and unusual prior approval and prior notice requirements for future transactions (regardless of the size of those transactions or whether they are reportable under the Hart-Scott-Rodino ("HSR") Act).[4]

The FTC consent order requires JAB to seek prior *approval* from the agency to purchase any clinic located within 25 miles of a JAB clinic anywhere in the states of California and Texas (not just in the local markets at issue in the JAB/SAGE transaction). As a result, the FTC will be able to block future JAB acquisitions in these states merely by withholding its approval. Moreover, the FTC required JAB to provide prior *notice* in advance of acquiring any clinic within 25 miles of a JAB clinic located anywhere in the entire United States.[5] According to Holly Vedova, the FTC's Director of the Bureau of Competition, "Private equity firms increasingly engage in roll-up strategies that allow them to accrue market power off the Commission's radar," and "[t]he prior notice and approval provisions will ensure the Commission has full visibility into future consolidation and the ability to address it."[6]

A statement issued by the three Democrats on the Commission, and a separate one issued by the Commission's two Republicans, revealed an intense debate within the agency about how PE firm acquisitions should be evaluated. Echoing Director Vedova, the majority explained that "prior approval and nationwide prior notice provisions are one way that the FTC can more closely monitor the potentially unlawful dealmaking activities of companies like [JAB] that have repeatedly attempted acquisitions the Commission alleged were unlawful."[7] The Democrats went on to state that, "Provisions like the ones in this matter will also allow the FTC to better address stealth roll-ups by private equity firms like [JAB]."[8] While voting to approve the settlement, Republican Commissioners Phillips and Wilson took issue with the broad prior approval and notice provisions and the "majority's evident distaste for private equity as a business model," writing that "[i]mposing heightened legal obligations on disfavored groups–including private equity–because of who they *are* rather than what they have *done* raises rule of law concerns."[9]

With a 3-2 majority for the Democrats firmly in place at the FTC, PE firms seeking settlements to resolve antitrust concerns related to their transactions should expect the agency to leverage new tools, such as broad prior approval and prior notice requirements.

AGENCIES CONSIDERING NEW APPROACHES TO ANALYZING PRIVATE EQUITY ACQUISITIONS

The agencies have also indicated that they are evaluating new approaches to analyzing acquisitions made by PE firms. For example, in a recent speech, FTC Commissioner Rebecca K. Slaughter expressed concern about "acquisitions by private equity firms in which the goal of the merger is for the acquirer to extract value from its target not by operating the asset and competing, but by executing a roll-up strategy."[10] Commissioner Slaughter went on to explain that such strategies are "[d]riven by a singular goal of extracting outsized financial returns for themselves and their investors" and "typically entail[] loading up the acquired company with unsustainable debt," which often leads to the acquired company exiting the market and no longer competing.[11] While acknowledging that such acquisitions are "not something our current antitrust theories contemplate", Commissioner Slaughter indicated that she believed such transactions may be able to be challenged using the "less familiar" second prong of Section 7 of the Clayton Act, which focuses on acquisitions that "tend to create a monopoly" in the remaining market.[12] DOJ Assistant Attorney General Jonathan Kanter has also signaled interest in challenging PE firm roll-ups, describing them as "often very much at odds with the law, and very much at odds with the competition we're trying to protect".[13]

As the FTC and DOJ continue to explore new approaches to analyzing PE firm acquisitions, it will be important to monitor whether any new theories are incorporated into the agencies' revised merger guidelines. In the meantime, PE firms should prepare for increased scrutiny of their acquisitions, possibly under novel theories that have not been used by the agencies in prior cases or been litigated in court.

AGENCIES SIGNALING INCREASED SECTION 8 ENFORCEMENT AGAINST INTERLOCKING DIRECTORATES

Both the FTC and DOJ have also indicated that increasing enforcement of Section 8 of the Clayton Act, which prohibits interlocking directorates on the boards of competing companies, will be a top priority going forward. In June 2019, the FTC issued a blog post stating that "there are unexpected restructuring and acquisition circumstances through which companies and their boards can wake up one morning to find themselves in a potentially problematic interlock situation."[14] The FTC singled out PE, explaining that "firms that acquire board seats across a diverse portfolio of companies may be particularly likely to encounter Section 8 issues via a merger or acquisition."[15]

Recent statements from top DOJ officials suggest that Section 8 scrutiny is only intensifying. In April 2022, AAG Kanter stated that "[f]or too long, our Section 8 enforcement has essentially been limited to our merger review process. We are ramping up efforts to identify violations across the broader economy, and we will not hesitate to bring Section 8 cases to break up interlocking directorates."[16] Similarly, in a June 2022 speech, Deputy Assistant Attorney General Andrew Forman expressed his desire to take "aggressive action" to limit board interlocks created by PE firm investments in competitors.[17]

Section 8 prohibits any "person" from serving as an officer or director of two competing companies.[18] While Section 8 has narrow exceptions, interlocking directorates are *per se* illegal and there need not be actual harm to competition for a violation to occur. PE firms should be aware that, while the case law is not settled on the issue, U.S. antitrust enforcers take the position that Section 8 "prohibits not only a person from acting as officer or director of two competitors, but also any one **firm** from appointing two different people to sit as its agents as officers or directors of competing companies . . . ."[19]

KEY TAKEAWAYS FOR PRIVATE EQUITY FIRMS

Based on these public statements, we are likely to see a significant uptick in DOJ and FTC investigations into interlocking directorates both as part of HSR merger reviews and on a standalone basis. In particular, PE firms that appoint directors to boards of companies that may be viewed as competing by U.S. antitrust enforcers are likely to face heightened scrutiny. As part of these investigations, we expect the agencies will also look to uncover whether any problematic information sharing is taking place between members of different boards of directors. Thus, PE firms should be aware of the agencies' increased interest in this area and work with antitrust counsel to avoid Section 8 issues and/or to develop strategies for responding to agency investigations.

DOJ and FTC leaders have made increasing antitrust scrutiny of PE firms a top priority. Accordingly, PE firms should expect the agencies to continue to use new tools and to explore new theories when analyzing, challenging and remedying their acquisitions. They should also prepare for a significant increase in the number of investigations and challenges of Section 8 violations the agencies pursue. As agency scrutiny continues to intensify, PE firms should engage with antitrust counsel to ensure they account for all important developments in this evolving area of antitrust enforcement.

New York
Worldwide Plaza
825 Eighth Avenue
New York, NY 10019-7475
+1-212-474-1000

London
CityPoint
One Ropemaker Street
London EC2Y 9HR
+44-20-7453-1000

www.cravath.com

[1] Statement of Chair Lina M. Khan Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya, In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Associates, Inc., and SAGE Veterinary Partners, LLC, File No. 211 0140 (June 13, 2022) [hereinafter Khan Statement], https://www.ftc.gov/legal-library/browse/cases-proceedings/public-statements/statement-chair-lina-m-khan-joined-commissioner-rebecca-kelly-slaughter-commissioner-alvaro-m-bedoya.

[2] FTC Acts to Protect Pet Owners from Private Equity Firm's Anticompetitive Acquisition of Veterinary Services Clinics, Fed. Trade Comm'n (June 13, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-acts-protect-pet-owners-private-equity-firms-anticompetitive-acquisition-veterinary-services.

[3] Complaint, In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Associates, Inc., and SAGE Veterinary Partners, LLC, File No. 211 0140 (June 13, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/2110140C4766NVASAGEComplaintPublic.pdf.

[4] Analysis of Agreement Containing Consent Orders to Aid Public Comment, *In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Associates, Inc., and SAGE Veterinary Partners, LLC*, File No. 211 0140 (June 13, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/2110140C4766NVASAGEAAPC.pdf.

[5] *Id*.

[6] FTC Acts to Protect Pet Owners from Private Equity Firm's Anticompetitive Acquisition of Veterinary Services Clinics, Fed. Trade Comm'n (June 13, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-acts-protect-pet-owners-private-equity-firms-anticompetitive-acquisition-veterinary-services.

[7] Khan Statement, supra note 1.

[8] *Id*.

[9] Concurring Statement of Commissioners Noah Joshua Phillips and Christine S. Wilson, *In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Associates, Inc., and SAGE Veterinary Partners, LLC*, File No. 211 0410 (June 13, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/2110140C4766NVASAGEPhillipsWilsonConcurringStatement.pdf.

[10] FTC Commissioner Rebecca K. Slaughter, Storming the Concentration Castle: Antitrust Lessons from the Princess Bride, Fed. Trade Comm'n (Mar. 31, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/Lastowka%20Lecture%203.31.22%20FINAL%20%28PDF%20Version%29.pdf.

[11] *Id.*

[12] *Id.* (Commissioner Slaughter explained that "The effect of [such a] transaction is to create a monopoly in the market, even though the merger of the PE firm and the target does not, by itself, substantially lessen competition because the PE firm was not previously competing in that market."); see also Letter from Sen. Elizabeth Warren et al. to Jonathan Kanter, Assistant Att'y Gen., Antitrust Div., U.S. Dep't of Just. (June 21, 2022), https://assets.law360news.com/1505000/1505209/2022.06.21%20letter%20to%20doj%20on%20reckitt%20benckiser%20sale%20to%20private%20equity.pdf (urging DOJ to "closely examine any private equity-backed deal . . . involving firms with checkered acquisition histories that are likely to hollow out their targets and weaken competition" and indicating lawmakers believe Section 7 of the Clayton Act "may well apply to any private equity firm with a noted history of selling off assets, laying off workers, and loading companies up with debt—regardless of whether any competing companies are in the firm's investment portfolio").

[13] James Fontanella-Khan, *Private Equity Moves into the Antitrust Spotlight*, Fin. Times (May 23, 2022), https://www.ft.com/content/f222e618-dc96-4204-8a27-00e0a9316236.

[14] Michael E. Blaisdell, *Interlocking Mindfulness*, Fed. Trade Comm'n (June 26, 2019), https://www.ftc.gov/enforcement/competition-matters/2019/06/interlocking-mindfulness.

[15] *Id*.

[16] *Assistant Attorney General Jonathan Kanter Delivers Opening Remarks at 2022 Spring Enforcers Summit*, U.S. Dep't of Just. (Apr. 4, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-opening-remarks-2022-spring-enforcers.

[17] *Deputy Assistant Attorney General Andrew Forman Delivers Keynote at the ABA's Antitrust in Healthcare Conference*, U.S. Dep't of Just. (June 3, 2022), https://www.justice.gov/opa/speech/deputy-assistant-attorney-general-andrew-forman-delivers-keynote-abas-antitrust.

[18] 15 U.S.C. § 19(a)(1) ("No person shall, at the same time, serve as a director or officer in any two corporations that are . . . competitors.").

[19] Michael E. Blaisdell, *Interlocking Mindfulness*, Fed. Trade Comm'n (June 26, 2019), https://www.ftc.gov/enforcement/competition-matters/2019/06/interlocking-mindfulness.